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C O N F I D E N T I A L SECTION 01 OF 02 BRASILIA 000043

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SUBJECT: LULA GETS STARTED - FIGHTING HUNGER ON A TIGHT BUDGET

REF: 02 BRASILIA 4561

Classified By: POLOFF RICHARD REITER FOR REASONS 1.5(b) AND (D).

1.(C) SUMMARY. President Lula,s administration is underway. At his first cabinet meeting on January 3, Lula emphatically focused his ministers both on combating hunger and on fiscal austerity. While the government's maneuvering room is circumscribed by the lack of a congressional majority and its financial limitations, Lula seems determined to chart a course that will address hunger, maintain fiscal discipline, and either build a stronger congressional coalition or find ways to do without it. END SUMMARY.

#### FIGHT AGAINST HUNGER IS JOB NUMBER ONE

2. (C) President Lula da Silva has never made a secret of his desire to attack hunger. He promised it during the campaign and in his election-night speech. His first post-electoral act in November was to set up the &Zero Fome8 (Zero Hunger) program headed by Jose Graziano, who now holds the title &Extraordinary (Ad hoc) Minister for Food Security and Combating Hunger.8 Graziano told us he intends to implement his nascent program in phases, beginning in the poorest areas of the northeast. He will not work alone. At the January 3 cabinet meeting, Lula directed each of his thirty-four cabinet-level officials to draft an anti-hunger strategy within thirty days.

3. (SBU) Even those ministries not normally associated with a social agenda are jumping aboard: Defense Minister Viega has pledged an anti-illiteracy program, Justice Minister Bastos will combat child prostitution, and Finance Minister Palocci will look to expand credit cooperatives. In fact, Lula announced that on January 10-11, he will take the entire cabinet to the poor backlands of the northeast to launch the Zero Fome program. With Congress out of session until mid-February, Lula carried out his first act by Presidential Decree (MP). MP 103, the first of this administration, formalizes a number of bodies in the President's Office, including a Food Security Council (CONSEA) to develop anti-hunger policies.

#### A CAP ON SPENDING - DESPITE PLEAS FROM THE STATES

4. (SBU) Combating hunger takes money, but the GoB does not appear inclined to deviate from its austerity program. The Ministries, anti-hunger projects will have to come from reprogramming existing funds, not new resources. Since November, Lula has been inundated by pleas for financial help from cash-strapped states, many of them politically-critical to his coalition, yet he has stayed the course. The richest states tend to be the squeakiest wheels: Rio Grande do Sul will be forced to slash its budget by 18%, while Minas Gerais faces a deficit of R\$700 million.

5. (SBU) But the biggest headache may be the state of Rio de Janeiro (septel), which is now behind both on its debts to the federal government and the salaries of its state employees. After Rio missed several scheduled debt payments to the federal treasury in recent weeks, the GoB first froze financial transfers from Brasilia to the state and then withdrew R\$ 86 million from the state's bank accounts (per a clause in the loan contract). This prompted newly-inaugurated Rio Governor Rosinha Garotinho to go to the Supreme Court to try to unblock the financial transfers while calling the GoB,s actions &a declaration of war on Rio8. The episode is significant because Garotinho,s Brazilian Socialist Party (PSB) is a member of the PT's congressional coalition. Rio gave Lula 79% of votes in October's presidential runoff, his greatest support from any state --in part due to Garotinho's support. Rosinha has attributed this episode to a long-running PSB/PT feud in the state, as Rosinha,s husband, Anthony Garotinho, ran against Lula for the presidency at the same time as Rosinha defeated the PT,s Benedita da Silva for the Rio statehouse. The PSB/PT dispute will likely be patched up, but it provides a telling example of how financial scarcity and local political antagonisms can weaken the PT,s coalition. It is also a measure of Lula,s resolve to limit spending, even to key allies.

#### FIGHTER PLANES IN A HOLDING PATTERN

16. (SBU) Another example of the GoB,s early commitment to austerity is the decision to delay purchase of twelve fighter planes for the Brazilian Air Force to replace its aging Mirage jets. Instead of choosing a vendor for the roughly \$800 million contract, new Defense Minister Viegas has announced that the purchase will be postponed for a year, cutting it close for the Mirages, scheduled to go out of service in 2005. As the planes were to be purchased through financing, the postponement will not free up funds, but it will avoid locking the administration into a huge commitment in its first weeks in office. Viegas may now consider purchasing used aircraft, which could improve the chances for the package of used F-16s that is among the bidders.

IN CONGRESS, &THE CLASSES COME LATER8

17. (SBU) The new Congress will not get down to work until February 17, giving the administration six weeks to try to secure a majority in both houses by bringing the PMDB party into the coalition. While talks with the PMDB fell apart before Christmas (reftel), both sides seem willing to keep trying and say they are committed to abiding by a side deal by which the PT will support the candidacy of a PMDB member for Senate President if the PMDB supports the PT candidate for Chamber President. The PMDB is a difficult party to negotiate with because of its internal rifts, so any deal will likely have to wait until its leadership elections on January 30.

18. (SBU) Lula is working on a &Plan B8 if the PMDB talks fall through. Like Presidents Sarney and Collor before him, Lula may try to mitigate his lack of a congressional majority by relying on public pressure and his own popularity to short-circuit congressional opposition. The PT has always used &assemblyist8 fora to bring different sectors and players to a common table. From this impulse sprang the Economic and Social Development Council (CDES) --also legalized by MP 103 (above). CDES brings together 82 business, labor, and civic leaders in a sort of Brazilian &social pact8. The GoB hopes to use it as a mechanism for the public to ratify its policies and thus force Congress to support its agenda. Tarso Genro, former PT Mayor of Porto Alegre, will be Lula,s Special Secretary for CDES; and Luiz Dulci, the Secretary-General of the President's Office, will work closely with him and with civil society. CDES will reportedly focus first on pension reform.

19. (SBU) But mindful that neither President Sarney nor Collor maintained his congressional support after the flush of electoral victory dissipated, Lula surely would prefer a real congressional majority to an evanescent social pact. Congress can be a tough place for a president without a majority. Or, as one wit noted while Lula received his Presidential certificate at the Congressional inauguration ceremony, &Lula needs to remember that the presidential diploma comes first, but the classes come later.8

COMMENT

10. (C) Lula must be doing something right. This week the Brazilian real strengthened to below R\$3.40 to the dollar for the first time since mid-September --before the first round of elections. The GoB,s reassuring economic team and steady drumbeat of austerity rhetoric appear to have calmed the markets. While the political and financial dragons still lie before him, Lula appears to have the sound instinct and steady nerves it will take to tame them.

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